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June 20, 2006

AGENDA ITEM 8

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

- I. SUBJECT:** Medicare Part D Options for 2007
- II. PROGRAM:** Health Benefits
- III. RECOMMENDATION:** Staff recommends, given recent legislative actions, that for 2007, CalPERS apply for the Retiree Drug Subsidy (RDS) consistent with the Board's actions regarding Medicare Part D for calendar year 2006.

IV. BACKGROUND:

The Medicare Prescription Drug, Improvement, and Modernization Act established a voluntary prescription drug benefit program (Part D) effective January 1, 2006.

Recent legislative action in the Budget Conference Committee related to the CalPERS request for administrative expenditure authority for Part D funds would significantly restrict the options available to CalPERS for 2007. Further details on this action are below in the section titled "Recent Developments." This legislative action is the reason the staff recommendation in this agenda item differs from the staff recommendation in May 2006. Rather than recommending CalPERS participate in Part D through the health plan based Prescription Drug Plan (PDP) option, staff is recommending that CalPERS apply for the Retiree Drug Subsidy (RDS) for 2007.

At the April 2006 Health Benefits Committee (HBC) meeting, staff presented an information item comparing two potential CalPERS Part D options for 2007: applying for the RDS or using health plan based Prescription Drug Plans (PDPs). Under both options, CalPERS would continue to provide the Kaiser Medicare Advantage-Prescription Drug (MA-PD) plan for Kaiser Senior Advantage enrollees, and would apply for the RDS for unassigned Kaiser enrollees (those over 65 and in the Basic plan). The analysis included the total net revenue available under each option, after deducting administrative costs. The estimate showed the same total net revenue for both options.

At the May 2006 Health Benefits Committee meeting, staff presented potential uses of federal reimbursement under the health plan based PDP option for CalPERS

Medicare-supplement plans. The analysis included the impact of the health plan based PDP option on Medicare-supplement rates, prescription drug co-payments, employers, and enrollees. Staff recommended for 2007 that CalPERS:

- Participate in Part D through the use of health plan based PDPs for members not enrolled in Kaiser Senior Advantage
- Continue the Kaiser MA-PD plan for Kaiser Senior Advantage enrollees
- Use PDP funding to reduce prescription drug co-payments and Medicare-supplement premiums

The May 2006 agenda item also summarized differences in disbursement flexibility between the RDS and PDP options:

- Under the RDS option, CalPERS would continue to deposit RDS payments into an escrow-type account, pending its receipt of a previously requested Attorney General's opinion and Board action based on that opinion. After receipt of the Attorney General's opinion, staff would present the Board with disbursement options for the RDS.
- Under the health plan based PDP option, the decision on the disbursement of PDP payments would not be dependent on the Attorney General's opinion.

The HBC deferred action and directed staff to provide more detail on the estimated revenue and administrative costs for each health plan under both options.

Recent Developments

1. Recent legislative action in the Budget Conference Committee related to the CalPERS request for administrative expenditure authority for Part D funds would significantly restrict the options available to CalPERS for 2007. The key provisions of the proposed budget control language dated June 6, 2006 (Attachment 1) include:
 - CalPERS shall apply for the RDS for 2007 consistent with its Part D actions for 2006 and deposit RDS payments in the Special Deposit Fund.
 - No funds remaining in the Special Deposit Fund after payment of CalPERS administrative costs may be spent or transferred to other funds except upon appropriation by the Legislature.
 - Funds attributable to contracting agencies remaining in the Special Deposit Fund after payment of CalPERS administrative costs shall be distributed to contracting agencies pursuant to a distribution schedule proposed by CalPERS and approved by the Director of Department of Finance.

- For any alternate approach regarding Part D subsidies for 2008, the Board shall submit a proposal to the Chair of the Joint Legislative Budget Committee, the chairs of the appropriate fiscal and policy committees of the Legislature, and the Director of Department of Finance by December 1, 2006.

Staff informed Board members about this legislative action on June 6, 2006 via facsimile from Gloria Moore Andrews, Deputy Executive Officer – Operations.

2. CalPERS sponsored legislation (SB 1729, Soto) designed to ensure that the Board has maximum flexibility for implementation of Medicare Part D. Current law restricts enrollment in the CalPERS Health Benefits Program to Medicare-eligible members enrolled in Part D or who are enrolled in a Board approved MA-PD (Kaiser). The pending legislation amends these restrictions to allow members to be enrolled in a Board approved MA-PD (Kaiser) or PDP. The Senate passed SB 1729 and referred the bill to the Assembly.

V. ANALYSIS:

In response to HBC requests at the May 2006 meeting, this analysis:

- Compares the estimated funds available under the RDS and the health plan based PDP options, for CalPERS Medicare-supplement plans, including administrative costs
- Provides more detail on the components of Medco Health Solutions' administrative costs

In addition, Attachment 2 recaps the disbursement choices under the health plan based PDP that staff presented at the May 2006 HBC meeting.

Estimated Funds Available and Administrative Costs

CMS bases payments under the RDS on 28 percent of drug costs between specified dollar thresholds (currently \$250 and \$5000 per individual) per calendar year, using claims experience for RDS-eligible members.

CMS calculates the reimbursement to PDPs using a national average of PDP bids for retiree prescription drug coverage, which CMS risk-adjusts based on the demographics of each group-enrolled client. **Based on the timing last year for announcement of the PDP national average bid, staff expects that CMS will publish the national average premium bid (for use in 2007) in September 2006.**

The following chart shows the estimated revenue from CMS, the administrative costs, and total net revenue for the two options for 2007, by health plan. Staff based revenue estimates on projections of 2007 enrollments (based on historical trends) and estimated CMS reimbursements.

PLAN	Retiree Drug Subsidy			Health Plan Based PDP		
	REVENUE	ADMIN COST	NET REVENUE	REVENUE	ADMIN COST	NET REVENUE
Blue Shield ⁽¹⁾	\$9,835,731	N/A	\$9,835,731	\$13,414,800	N/A	\$13,414,800
PERS Choice ⁽²⁾	\$15,806,240	\$191,440	\$15,614,800	\$20,919,127	\$4,149,018	\$16,770,109
PERSCare ⁽²⁾	\$31,629,430	\$347,114	\$31,282,316	\$37,930,072	\$7,522,903	\$30,407,169
WHA ⁽³⁾	\$194,005	\$0	\$194,005	N/A		
CalPERS Admin		\$439,000	-\$439,000		\$439,000 ⁽⁴⁾	-\$439,000
TOTAL	\$57,465,406	\$977,553	\$56,487,852	\$66,290,952	\$12,110,921	\$54,180,031

⁽¹⁾ Blue Shield estimates CMS reimbursement of \$50 per member per month under the PDP option. Blue Shield would absorb RDS administrative cost and account for PDP administrative cost in its existing overall administrative fees.

⁽²⁾ Medco estimates CMS reimbursement of \$54 per member per month under the PDP option. Under the RDS option, Medco would charge \$.55. See below for detail on Medco's PDP administrative cost.

⁽³⁾ Western Health Advantage would not have any RDS administrative cost. WHA did not file for a PDP contract for 2007. If CalPERS implements the plan based PDP in 2007, CalPERS would apply for the RDS for WHA members.

⁽⁴⁾ Staff expects PDP administrative cost to be equal to or less than RDS administrative cost.

Medco PDP Administrative Cost Detail

Medco provided the following explanation of the costs associated with administering the health plan based PDP option for PERS Choice and PERSCare.

Under the health plan based PDP option, Medco estimated the 2007 CMS reimbursement for PERS Choice and PERSCare at \$54 per member per month. Of that \$54, Medco's administrative fee would be \$11.92 pmpm containing a margin of \$1.54, or 12.9 percent, which represents between four and five percent of estimated 2007 drug spend. Unplanned work and/or communication requirements to implement changes based on CMS guidance are also funded out of this margin.

Of the \$11.92 pmpm (for non-pharmacy expenses), \$10.38 is Medco's 2007 CMS bid submission for plan-sponsored PDPs. This represents Medco's cost of providing PDP services without mark-up.

CMS-required services fall into two categories:

1. Member support - communications and services (\$5.86), which includes:
 - CMS-required marketing materials
 - Customer service calling costs
 - Medication Therapy Management Program
 - Reviews and appeals, including transition programs
2. Medco staff, operational support and account maintenance and systems support and setup (\$4.52), which includes:
 - Operational support (CMS reporting, financial management, account team support, and other operational activities)
 - Third party vendor fees (enrollment, premium reconciliation, certification, Low Income Subsidy (LIS) management)
 - Medicare required fees to support CMS systems development and to track the co-pays paid by each member to determine when a member enters the CMS mandated catastrophic coverage benefit stage.

VI. STAFF RECOMMENDATION:

Given the constraints of the budget control language, staff recommends for 2007 that CalPERS apply for the Retiree Drug Subsidy (RDS) consistent with the Board's actions regarding Medicare Part D for calendar year 2006.

VII. STRATEGIC PLAN:

The staff recommendation supports the Health Benefits Branch Three-Year Business Goal XI to "Promote the ability of enrollees and employers to make informed decisions resulting in improved lifestyle choices and health outcomes" by creating financial incentives for our enrollees to choose the least cost, most-effective pharmacy regimen.

In addition, the staff recommendation supports the CalPERS Strategic Plan, Goal X to "Develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers."

VIII. RESULTS/COSTS:

As shown on the chart under "Analysis", the estimated RDS payments for 2007 would be \$57.5 million with associated administrative costs of \$977,553, for total net revenue of \$56.5 million.

Sandra Felderstein, Chief
Office of Health Policy and Program Support

Terri Westbrook
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Health Benefits Branch

Attachments

PROPOSED BUDGET CONTROL LANGUAGE

June 6, 2006

California Public Employees' Retirement System—Item 1900-001-0942—Medicare Part D
Employer Subsidies

Provisions:

1. Funds appropriated in this item shall be used by the Public Employees' Retirement System to implement the processing of Medicare Part D eligibility files, reconciliation files, and subsidy requests. The Public Employees' Retirement System shall continue to apply directly for the maximum possible amount of Medicare Part D drug subsidies in 2006 and 2007.
2. Notwithstanding the requirements of Provision 1, the Public Employees Retirement System may choose not to apply for subsidies related to plans that are eligible to act as sponsors and receive Part D subsidies related to their enrollees, consistent with actions of the Public Employees' Retirement System for calendar year 2006. If the Public Employees' Retirement System chooses not to apply for subsidies pursuant to this provision, the Public Employees' Retirement System shall so notify the Department of Finance, the chairpersons of the committees and the appropriate subcommittees in each house of the Legislature that consider the State Budget, the Chairperson of the Joint Legislative Budget Committee, and the Legislative Analyst's Office, and shall include in that notification an explanation of the facts and circumstances underlying that choice.
3. All Medicare Part D drug subsidies received as a result of the applications made pursuant to Provision 1 shall be deposited to the Special Deposit Fund and identified as Medicare Part D drug subsidy funds. The Medicare Part D drug subsidy funds shall be expended for the purposes described in Provision 1. No Medicare Part D drug subsidy funds remaining in the Special Deposit Fund after payment of the uses listed in Provision 1 may be spent or transferred to other funds except upon appropriation by the Legislature. Notwithstanding this prohibition on spending or transferring the funds, the portion of any Medicare Part D drug subsidy funds that (1) are attributable to public employers other than the state that participate in the Public Employees' Retirement System's health programs and (2) remain in the Special Deposit Fund after paying for the activities described in Provision 1 shall be distributed to these other public employers pursuant to a distribution schedule proposed by the Public Employees' Retirement System and approved by the Director of Finance.
4. If the Board of Administration of the Public Employees' Retirement System wishes to propose an amended approach concerning applications for Medicare Part D drug subsidy funds in 2008 or a use for Medicare Part D drug subsidy funds expected to be accumulated in the Special Deposit Fund, the Board of Administration shall submit a proposal for these purposes to the Chair of the Joint Legislative Budget Committee, the chairs of the appropriate fiscal and policy committees of the Legislature, and the Director of Finance on or before December 1, 2006.

Choices Under Plan Based Prescription Drug Plan (PDP) Option

As presented at the May 2006 Health Benefits Committee meeting, the three choices for use of PDP funds under health plan based PDPs are:

1. Premium reduction only: PDP buy-down of premiums
2. Prescription drug co-payment reduction only: PDP buy-down of prescription drug co-payments with no change in premiums
3. Combination: PDP buy-down of prescription drug co-payments and premiums

Choice 1: *Premium Reduction*

Under this choice, CalPERS health plans would use their PDP payments to reduce Medicare-supplement premiums. Those benefiting from this choice include:

- State subscribers who pay out-of-pocket expenses toward their monthly Medicare-supplement premium and/or their Medicare Part B premium
- Contracting agency enrollees who receive less than 100 percent premium coverage as a retiree benefit
- Contracting agencies that cover a percentage of retiree health benefit premiums
- State of California: when the Medicare-supplement plus Part B premium is less than the state employer contribution (a lower premium would increase the differential)

The following employers and enrollees, however, will not realize any benefit from reduced Medicare-supplement premiums:

- Contracting agencies that contribute a flat rate toward retiree premiums
- Contracting agency enrollees who receive 100 percent Medicare-supplement premium coverage as a retiree benefit
- State enrollees who do not contribute toward their monthly Medicare-supplement and Medicare Part B premium

Staff does not believe that this choice provides a good balance between benefits to both our members and employers.

Choice 2: *Prescription Drug Co-payment Reduction*

Under this choice, CalPERS health plans would use their PDP payments to reduce Medicare prescription drug co-payments without impacting the Medicare-supplement premiums.

This option would provide no premium savings to the State of California and contracting agency employers, and would result in unique prescription drug co-payments for each health plan.

Choice 3: Combination of Reduced Prescription Drug Co-payments and Reduced Premiums

Under this choice, for Medicare, CalPERS health plans would eliminate generic prescription drug co-payments (currently \$5 for retail purchases and \$10 for mail order) and reduce brand formulary co-payments on retail purchases to \$10 (currently \$15) and mail order to \$15 (currently \$25). The co-pay changes encourage enrollees to use generic and formulary drugs.

Kaiser's Senior Advantage Plan and Western Health Advantage (WHA) would adopt this co-payment structure to provide parity across all Medicare plans. Because Kaiser has already accounted for its Medicare Part D funding in its proposed 2007 rates, its single party monthly Medicare rate would increase by \$24 as a result of this co-payment structure change. Because WHA is not participating in a plan based PDP, its single party monthly Medicare rate would increase by \$26 as a result of this co-payment structure change.

Under this choice, WHA would need Department of Managed Health Care (DMHC) approval to change its prescription drug co-payments. Staff expects WHA would quickly receive approval from DMHC, so this requirement would not present a barrier to implementation.

Reducing prescription drug co-payments and Medicare-supplement premiums combines the benefits of both choices described above, offering the broadest array of benefits to both employers and enrollees.

Staff will provide the 2007 Medicare-supplement premiums under this option at the June 2006 HBC meeting.